U7475-2

May 1989 Monthly Survey

June 8, 1989

Surveys of Consumers

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Consumer Confidence Continues On Soft Landing Approach

Index Continues to Slip

The Index of Consumer Sentiment was 90.7 in the May 1989 survey. Although this was less than one Index-point below the 91.5 recorded in April, it marked the fourth consecutive small monthly decline since the start of the year. The cumulative decline represents a significant loss from the 97.9 recorded in January 1989. Whereas the January 1989 Index figure was the highest recorded in more than a year, the May was the lowest since the end of 1987.

Despite the recent declines, the Index remains at relatively favorable levels. The May 1989 survey marked the completion of the sixth year since the Index first rose above 90, marking the longest period of favorable readings since the 1960s.

Since May of 1983 the Index has remained in a narrow range: the Index fell below 90 in only six of the 73 months and rose above 98 in only six of the 73 months. Moreover, the past six years has been marked by repeated shifts from the upper to lower ends of this narrow range.

It is clear that the recent trends in consumer sentiment indicate a cooling in demand. However, whether it signifies the start of a more persistent downward decline is not yet clear.

Among families with incomes of $40,000 or more, the Index stood at 100.3 in the May survey, slightly above the 99.8 recorded in April and the 100.0 recorded in March, but below the January 1989 reading of 106.8.

Loss Centered in Expectations Component

The entire decline in the May survey was concentrated in the expectations component of the Index rather than in evaluations of current economic conditions. The Index of Consumer Expectations, the component of the Index of Leading Indicators, fell to 80.1 in May, down from 83.2 in April and 89.9 in January 1989. The loss since the start of the year has been the result of weakening prospects for the general economy.

In contrast to weakening expectations, evaluations of current economic conditions improved in the May survey. The Current Conditions Index rose to 107.1 in the May survey from 104.4 in April, and was just above the 106.5 recorded in May 1988. Consumers' evaluations of their personal financial situation have remained positive, showing little change since the start of the year.

Weakening Prospects for Economy Reported

Since the start of the year, consumers' evaluations of the strength of the national economy have weakened. In the May 1989 survey, the proportion of families that thought the national economy had improved during the past year fell to 44 percent from 56 percent at the start of the year.

For the year ahead, good times financially in the country as a whole were expected by 46 percent of all families in the May 1989 survey, down from 56 percent in January. The long term outlook for the economy also worsened, with the proportion of consumers that expected good times financially over the next five years falling to 36 percent in May 1989 from 45 percent in January.

Unemployment Expected To Remain Unchanged

Half of all families in the May 1989 survey (52 percent) expected the national unemployment rate to remain largely unchanged at its current level during the year ahead. Given that the unemployment rate is now at record lows, this is certainly a positive outlook. Nonetheless, compared with a year ago fewer families expected the unemployment rate to remain unchanged and more families expected it to increase during the year ahead. In the May 1989 survey, 35 percent expected increases in the national unemployment rate, up from 21 percent one year earlier.

Interest Rate Concerns Lessen

The May 1989 survey recorded the first substantial decline in interest rate expectations since the start of the year. Among all families in the May 1989 survey, 64 percent expected interest rate increases during the year ahead, down from the all-time peak of 75 percent recorded in April. Although this still leaves interest rate expectations at unfavorable levels, it is the first substantial break in the upward trend.

Home Buying Attitudes Post Small Improvement

Favorable attitudes toward buying conditions for homes were held by 61 percent of all families in the May 1989 survey, up somewhat from the 58 percent recorded one month earlier but well below the 72 percent recorded one year earlier.

The small May improvement was due to more favorable perceptions of home prices. Favorable references to current home prices were made by 22 percent of all families in May, up from 17 percent in April, while complaints about high home prices fell to 13 from 16 percent one month earlier.

Changing perceptions of interest rate trends were reflected in fewer consumers mentioning the advantage of borrowing in advance of rising interest rates, falling to 15 in May from 20 percent in April. Thus the initial reactions of consumers to interest rate declines have a negative impact on home buying attitudes, as consumers are more likely to postpone purchases in anticipation of further declines.

Vehicle Buying Attitudes

Attitudes toward buying conditions for vehicles weakened slightly in the May survey. The recent round of price and interest rate discounts offered by vehicle manufacturers had only a small and short-lived impact. The proportion of families holding favorable vehicle buying attitudes slid back to 63 percent in May from 65 percent in April. References to the availability of price discounts fell to 29 percent in May from 32 percent in April, while mentions of interest rate discounts fell to 23 from 25 percent. Overall, vehicle buying attitudes in the May 1989 survey were nearly identical to those recorded a year earlier.

The reaction of consumers to the recent round of price and interest rate discounts indicates the

declining influence of these sales incentives. In part this is due to the expectation that such discounts will be more or less continuously available.

Buying Conditions for Durables

Favorable attitudes toward buying conditions for furniture, appliances, and home electronic goods were held by 73 percent of all families in the May 1989 survey, down from 75 percent one month earlier and 79 percent one year earlier. The small declines recorded during the past year still leave these buying attitudes at very favorable levels. When asked to explain their view, fewer families mentioned the availability of price discounts on these large household durables.

Personal Finances

The May survey recorded mixed changes in consumer's evaluations of their personal finances. Consumers' evaluations of their current financial situation improved somewhat, while prospects for future changes in their financial situation dimmed. Both changes, however, were relatively small.

Among all families, 45 percent reported that their financial situation had improved during the past year, up from 42 percent one month earlier and 40 percent one year earlier. The small recent improvement was due to less frequent complaints that rising prices had lowered their standard of living (12 percent in May, down from 16 percent in April).

The proportion of families that expected their financial situation to improve during the year ahead slipped to 39 percent in May from 41 percent in April, but remained above the 36 percent recorded one year earlier. The most common expectation was that their personal financial situation would remain largely unchanged during the year ahead, reported by 45 percent of all families in the May 1989 survey. Although just 14 percent of all families expected their finances to worsen in the May 1989 survey, this was up from 11 percent one month earlier and 9 percent one year earlier.

Inflation Fears Mount

In the May 1989 survey, consumers expected an annual rate of inflation of 5.8% during the year ahead, up sharply from the 5.0% recorded in April and the 4.9% recorded in May of 1988. The May 1989 reading of 5.8% was the highest expected inflation rate recorded in more than five years.

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The May 1989 survey included 503 completed interviews conducted between May 1 and May 26, 1989.